PEOPLE'S BANK
v
MANNUEL ENTERPRISES (PVT) LTD.

SUPREME COURT
FERNANDO, J.
J.A.N. DE SILVA, J.
JAYASINGHE, J.
SC CHC 19/98
HC (CIVIL) WP 138/96 (1)
AUGUST 8, 2003
SEPTEMBER 1, 2003

Money due on trust receipts – Right of the Bank to set off monies in a current account against a loan account – Prescription Ordinance sections 6, 12 – Could the plea of prescription be defeated by any part payment of interest/principal sum by defendant ? Could the creditor appropriate part of the debt from the customer's account and claim that, it is a payment by the debtor to overcome the limitation rule ?

The appellant People's Bank instituted action against the defendant on seven causes of action - on specific trust receipt loans. The defendant-respondent took up the position that the seven causes of action are prescribed. The bank contended that, the bank had the right to deduct any sum of money from any account other than the account referred to in the agreement for the payment of monies due on the trust receipt. It was the position of the bank, the Banker had an undisputed right to set off unless there is an agreement to the contrary.

The bank also contended that, whatever monies that came to the K account was collected into a Margin account by the bank and appropriated periodically of all trust receipt loans and in such circumstances, the claim is not barred by prescription.

Held:

(1) A banker has an undisputed right to set off unless there is an agreement to the contrary.

(2) On an examination of all the trust receipt loans - it is clear that there is an express clause whereby parties have agreed that the bank is authorized to debit only the current account X of the Colombo Branch.

In view of this express agreement bank had no right to deduct any sum of money from any account other than the account referred to in the agreement for the payment of monies due on the trust receipt.

Therefore any deductions or set off made from the account of the defendant from the K account was not valid, illegal and arbitrary.

(3) The prescriptive period is 6 years. The trust receipt loans were given for a 90 day period and the cause of action would arise after the expiration of the time limit.

(4) The effect of a part payment in circumstances from which a promise to pay the balance may legitimately be inferred, is to take the case out of the operation of the statute. The law in the absence of anything to the contrary implies a promise to pay the balance even if the debtor was already prescribed.

(5) The defendant has not done any positive act to effect payment to bring the claim within the prescriptive period. The creditor cannot appropriate part of the debt from the customers account and claim that it is payment by the debtor to overcome this limitation rule.

Per Asoka de Silva, J.

"Next question is can a banker exercise the right of set off in respect of a debt which is time barred ? The answer is the affirmative. The law of prescription suppresses the remedy it does not kill the right. The creditor can recover it but he cannot file a suit. The creditor can exercise a right of set off if it is available."

APPEAL from the judgment of the Commercial High Court of Colombo.

Cases referred to:

(1) *Halisowen Press Assemblies Ltd.*, v *Westminster Bank* – 1970 3 WLR 625

(2) *Garnett* v *M'kewanp* 1872 LX 8 x 10

(3) *Buckingham and Company* v *London and Midland Bank Ltd.* – 1895 12 TLR 70

(4) *Bradford Old Bank Ltd* v *Sutcliff* – 1978 2 KB.

(5) *Green Halge and Son* v *Union Bank of Manchester* – 1961 – 1 All ER 197

(6) In Re Halisown - 1971 All ER 641 (HL) Overturned the decision of the Court of Appeal in 1970 3 WLR 625 – 1 above)

(7) *Bastian Silva* v *William Silva* – 55 NLR 347 at 348

(8) *Moorthipillai* v *Siva Kaminathan* – 14 NLR 30

(9) *Arunasalam* v *Ramasamy* – 17 NLR 156

Rohan Sahabandu for plaintiff-appellant

Nihal Jayamanne PC with *Lakshman Perera, Udisa Caldera* and *Dilhan de Silva* for defendant-respondent.

Cur.adv.vult.

December 19, 2003

J. A. N. DE SILVA, J.

This is an appeal by the appellant-plaintiff bank against the decision of the Commercial High Court Judge whereby the plaintiff's action was dismissed by the said High Court Judge on the ground of prescription. This action was instituted in the District Court of Colombo, but was subsequently transferred to the Commercial High Court with the establishment of that Court.

The appellant-plaintiff bank (hereinafter referred to as plaintiff) on or about the 20th March 1996 instituted action against the defendant respondent setting out seven causes of action each concerned with the default in payment by the defendant respondent of specific Trust Receipt Loans together with interest. These Trust Receipts were marked as P1, P4, P7, P10, P13, P16 and P19 and the plaintiff Bank claimed the following sums.

(a) Rs. 2,924,456/76 together with interest at the rate of 25% per annum on a sum of rupees 1,119,000/-, from 1st August 1995 onwards in respect of 1st, 2nd, 3rd and 4th causes of actions, and

(b) Rs. 2,340,326/03 together with interest at the rate of 26% per annum on a sum of Rs. 925,000 from 1st August 1995 onwards in respect of 5th, 6th and 7th causes of action.

It was the position of the plaintiff bank as set out in the plaint that

(a) The defendant-respondent was a customer of the Bank and maintained two current accounts one at the bank's Foreign Branch at Fort and the other at the Kurunegala Branch.

(b) All Trust Receipts Loans were granted to the defendant respondent between 17th July 1987 and 13th November 1987.

(c) The entire capital amounts advanced in respect of the said Trust Receipt Loans referred to in the 1st cause of action remained due and unpaid by the defendant-respondent.

(d) The defendant-respondent paid monies against the said 7 loans from time to time during the period 21st August 1989 to 16th September 1995. Such sums had first been paid into a margin account and thereafter the bank appropriated the same to deduct interest and BTT that had accrued in respect of the said loans.

(e) Such payments by the defendant-respondent had accounted for the settlement in full the interest due up to 1st October 1989 on the loans referred to in the 1st, 2nd, 3rd and 4th causes of action and the interest up to 12th September 1989 on the loans referred to in the 5th, 6th and 7th causes of action.

(f) Such payments by the defendant-respondent also served to take the said causes of action out of the operation of the law of prescription and

(g) The defendant respondent failed and neglected to pay the monies due on the said seven Trust Receipts since 1993 although demanded by the plaintiff bank.

The defendant-respondent in its answer admitted applying and obtaining the said Trust Receipts Loans but took up the position that the seven causes of action were prescribed in law. The learned High Court Judge by his judgment dated 17th March 1998 dismissed the plaintiff's action by deciding all the issues in favour of the defendant including the issue raised on prescription.

At the hearing of this appeal two main questions came up for consideration. Firstly whether the bank could set off monies in a current account against a loan account and secondly could the prescription period be defeated by any part payment of the loan or interest by the customer.

Learned counsel for the plaintiff-appellant relied on several authorities in support of this proposition that a bank has the right to combine two accounts whenever it pleases and to set off against the other if there was no express or implied agreement to the contrary. He cited the following passage from the book "Bankers remedy of set off" 1993 (Butterworth Sydney Australia) where Prof. Goode has this to say, "the law of set off assumed a large imbalance in modern finance and commerce. It is in substance though not in law a form of security by which a creditor is able to restore to self help, setting off the debt due to him against a debt due from him to the other party."

It is to be noted that the right to set off is also known as the right of combination of accounts. A bank has a right to set off a debt owing to a customer against a debt due from him. It is a valuable right and sometimes it is also treated as the right to lien. It is well settled law that the monies deposited with the bank becomes its own money and the only obligation of the bank is to pay the equivalent amount on demand by the customer. In case of money, lien of the bank is not applicable; whenever a bank receives a cheque or bill or warrant for collection it has a lien on the specific movable, but as soon as the bank collects it and credits the process to the customer's account it cannot be said that the banker has a lien on the money so credited. Though the bank has no lien yet it has the right to set off debt in one account of the customer against the credit in another account. This right although has been derived from lien is not a lien. Lord Denning in *Halesowen Press Work Assemblies Limited* v *Westminster Bank Limited* (1) observed thus. "In order to avoid confusion, I think we should discard the word 'lien' in this context and speak simply of a banker's right to combine accounts or right to 'set off' one account against the other."

There are several decided cases where the right of a bank to 'set of' has been recognized and applied. In *Garnett* v *M'kewn* (2) a customer who had two accounts with different branches of a bank drew cheques against his credit balance at one branch of a bank. At another branch he was indebted to an amount almost as great as the credit balance at the first and the bank without notice to him combined the balances and dishonored the cheques. It was held that they were entitled to do so. The question whether the customer is entitled to notice was also considered at length in this case. *Buckingham and Company* v *London and Midland Bank Ltd.* (3) is another important case which considered the above question. This case provides an example of one of the principal exceptions to the banker's right to set off. The plaintiff had a current account and also a loan account secured against house and property. The branch manager had the property re-surveyed and decided that the advance was too high. He informed the plaintiff that his account had been closed. The plaintiff protested that he had cheques outstanding but the manager duly combined the accounts and dishonoured the cheques. The plaintiff filed action against the bank

and the court decided that the customer could draw upon the current account without reference to the loan account and was entitled to reasonable notice of the ending of this arrangement.

On the same question Scrutton L, J. in *Bradford Old Bank Limited* v *Sutcliff* (4) stated that "the sum paid into the current account are appropriated to that account and cannot be used by the bank in its charge of loan account without the consent of the customer." In *Green Halge and Son* v *Union Bank of Manchester Ltd.* (5) Swift, J. stated that if a banker agrees with his customer to open two or more accounts he has not in my opinion without the assent of the customer any right to move either assets or liabilities from one account to another".

Lord Denning did not agree with this broad dictum but having examined a long line of authorities expressed the view that a banker is entitled to combine two accounts unless there is an agreement to keep them separate. "A good instance is where a bank opens two accounts for a customer, one of which is a loan account... and the other is a current account... In such a case there is usually an implied agreement that the bank will not combine the two accounts or set-off one against the other, without the consent of the customer." In the same case Winn J. too subscribed to the same view. *Halisowen case* (6) went up to the House of Lords. Viscound Dilhorn, Lord Simon, Lord Crust, Lord Brunden over turned the decision of the Court of Appeal on the ground that there was no separate agreement implied or expressed to keep the accounts separate, but accepted the fact that a banker has an undisputed right to set off unless there is an agreement to the contrary.

The question therefore in the instant case is whether there was an agreement by the bank to keep the two account separate. On an examination of all the Trust Receipts marked in this case viz. P1, P4, P7, P10, P13, P16 and P19 it is clear that there is an express clause whereby parties have agreed that the bank is authorized to debit only the current Account No 100214 of the Foreign Branch of the Peoples Bank. In view of this express agreement bank had no right to deduct any sum of money from any account other than the account referred to in the agreement for the payment of monies due on the trust receipts. Therefore any deductions or set off made from

the account the defendant had in the Kurunegala Branch was not valid, illegal and arbitrary.

The second question that has to be considered is could the plea of prescription be defeated by any part payment of interest or principal sum by the defendant ?

It is accepted that the prescriptive period is 6 years (vide section 6 of the Prescription Ordinance). The Trust Receipt Loans were given for 90 days period and the cause of action would arise after the expiration of that time limit. This is evident from the following table.

TR Loans	Issued On	Due Date
TR 1	17.07.87	17.10.87
TR 4	20.07.87	20.10.87
TR 7	24.08.87	24.10.87
TR 10	17.09.87	17.12.87
TR 13	29.09.87	28.12.87
TR 16	23.10.87	23.01.88
TR 19	13.11.87	13.02.88

On an examination of the bank statements it is clear that not a cent has been paid back in respect of any loan by the defendant other than TR 1 where he has made a payment on 13.11.87. From time to time the bank has appropriated the monies that come in to the Kurunegala Branch Account of the defendant. The last of such appropriation has taken place on 03.03.1995. The letter of demand has been sent on 12.01.1996 and action had been instituted in 28.03.1996. The claim of the plaintiff's bank is that as the payments have been made upto 1995 action is well within time and not prescribed. On behalf of the defendant-respondent it has been submitted that the margin account statement produced by the bank does not indicate that money has been transferred from the defendant-respondent's Kurunegala account and the bank has failed to produce the statements relating to that account.

The legal consequences of payment in reduction of a debt are clear enough, and the application of principles involved is expressly provided for in a proviso to Section 12 of the Prescription Ordinance. These principles were carefully considered and applied by Gratiaen, J. in *Bastian Silva* v *William Silva* (7) in the following

terms "the effect of a part payment in circumstances from which a promise to pay the balance may legitimately be inferred, is to take the case out of the operation of the statute - *Moorthypillai* v *Sivakaminathan*[8]. As was explained in *Arunasalam* v *Ramasamy*,[9] the law in the absence of anything to the contrary, implies a promise to pay the balance, even if the debt was already prescribed."

"If a claim relates to a single debt which is prima facie statute - barred, the burden is on the creditor relying on the subsequent payments to show that it was made on account of debt and as a part payment." "If however there are more debts there are, the creditor must prove that the part payment was made "a general account" in order to defeat a plea of prescription in respect of all the items."

The learned counsel for the plaintiff bank contended that as monies have been paid periodically till 1995 the claim of the bank is alive and not barred by prescription. It is common ground that the defendant had not paid any money in respect of the Trust Receipts except the payment made on 13.11.87 as stated above. Whatever the monies that came to the Kurunegala account was collected into a margin account by the Bank and appropriated periodically in respect of all Trust Receipts Loans. Now the question arises as to whether these were payments by the defendant. It is obvious that the defendant has not done any positive act to effect payment to bring the claim within the prescriptive period. Can the creditor appropriate part of the debt from the customers account and claim that it is payment by the debtor and overcome the limitation rule ? Certainly not. Next question is can a banker exercise the right of set off in respect of a debt which is time barred ? The answer is in the affirmative. The law of prescription suppresses the remedy, it does not kill the right. The creditor can recover it but he cannot file a suit. The creditor can exercise a right to set off if it is available and there is nothing wrong with the same.

In the instant case as I have already held that there is no agreement between the parties to allow the bank to combine the accounts the prescription starts running from 90 days of issuing the Trust Receipts as the defendant had not paid any monies in respect

of the loan he obtained from the Foreign Branch in Colombo. In the circumstances the learned High Court Judge is correct in coming to the conclusion that the plaintiff's action is time barred.

For the above reasons this appeal is dismissed without costs. 220

M. D. H. FERNANDO, J. – I agree.

N. JAYASINGHE, J. – I agree.